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MORTGAGE BANKING

AUGUST 1985

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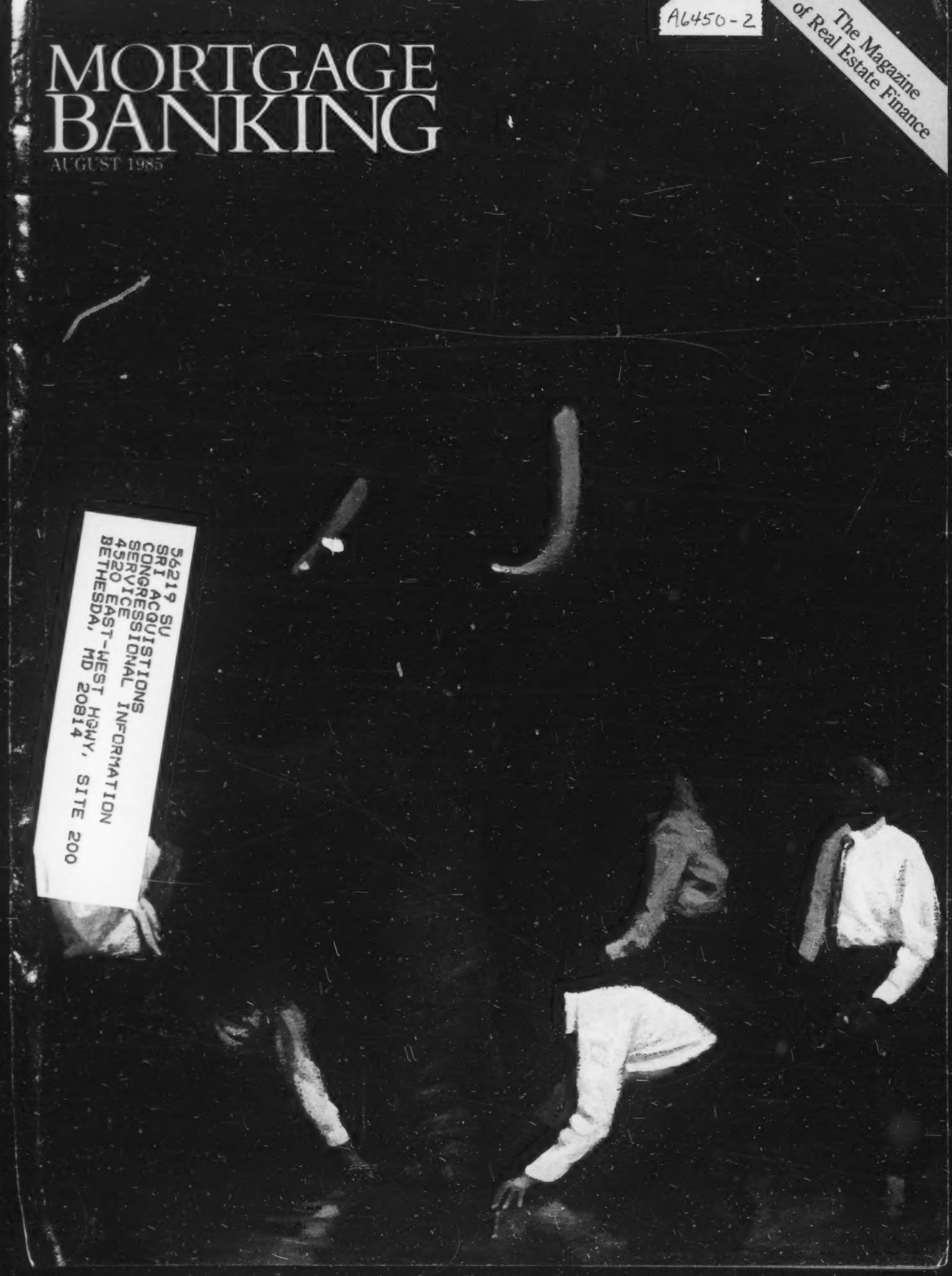

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MORTGAGE BANKING

ARTICLES

PAGE 8
SERVICING COSTS: PUTTING THE PIECES TOGETHER
Dr. Victor Cholewicki
To determine a firm's profitability, an analysis of the income and expense of a servicing operation must be made. This article contains extensive comparative servicing cost and income data for mortgage banking firms based on MBA's *Income and Cost for Originations and Servicing of 1-4- Unit Residential Loans, 1983.*

Page 24
GNMA SERVICING: PAYING THE PRICE
Herbert L. Carrel, CMB
GNMA servicing provides the best dollar for dollar value to a servicer and the highest prices are now being paid for GNMA servicing. But there are additional costs a servicer incurs that are not generally computed in cost and analysis.

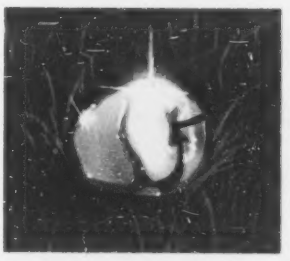
PAGE 42
STRATEGIC VIEW OF SERVICING EXPENSES
Chester R. Bear, Jr.
Because of inaccurate measuring standards or no standards at all, there is a misconception that bigger is always better and the more mortgage bankers get, the cheaper it becomes. There are many variables and what seems to be a high figure for one company might, in reality, be much more competitive if all of the components were the same.

PAGE 55
YIELD: THE REALISTIC WAY TO EVALUATE A MORTGAGE SERVICING PORTFOLIO
Hunter W. Wolcott
The most important task in fixed-income portfolio management is, and always has been, balancing risk and yield. Managing a portfolio of mortgages and mortgage pass-throughs is somewhat more challenging. Investing in servicing takes the challenge to the limit.

PAGE 63
BITING THE REO BULLET
Carole R. Adams and Jack W. Newton
It could be said that an REO was proof that somewhere along the line, somebody goofed. Lenders have "amortized" losses, preferring to hide the problem rather than face up to them and work out satisfactory solutions. No lender wants them; no lender likes them; but every lender has them.

PAGE 73
TAKING RISKS AND MAKING CHOICES
Peggy Crawford and Phyllis A. Garrity
An increasing number of homeowners are willing to accept the risks associated with ARMs. But, do borrowers fully understand the risk associated with the instruments they accept? How do borrowers evaluate the mortgage instruments available to them? Are the individuals who accept ARMs less risk averse than individuals who accept FRMs? These questions are addressed in this study.

PAGE 78
HARVEST TIME: LIMITED SECURITIES SUBSIDIARIES
Robert J. Corletta
The sale, packaging and participation in real estate limited partnerships are not exclusive to the Wall Street firms. For smaller financial services companies, mortgage banking companies and S&Ls, a limited securities broker/dealer firm may provide an additional profit center that is a natural extension of current operations.



PAGE 86
THE "YUPPIE MORTGAGE:" INSTRUMENT OF THE 1980s
Doug Gallagher
The yuppie mortgage loan results in an early payoff because it provides more frequent payments than a normal fixed-rate loan. There are approximately 26.09 payments made by a yuppie loan borrower compared to only 12 monthly payments on a fixed-rate mortgage. The combination of larger payments and an accelerated repayment with a yuppie loan produces a reduction in the term by one third.

PAGE 95
THE LAST WORD (UNKNOWNS OF ARM SERVICING)
Larry Litton
It is essential to track the performance of ARMs by the overall ARMs portfolio, as well as by individual ARM types. It is good management to maintain delinquency and foreclosure data by loan type.

DEPARTMENTS

PEOPLE	**101**
BOOKS	**105**
SECONDARY MORTGAGE MARKETS	**107**
MORTGAGE MARKET TRENDS	**109**
AD INDEX	**119**

SERVICING COSTS:

Putting The Pieces Together

By Dr. Victor Cholewicki

The increasing tendency to view servicing portfolios as marketable assets rather than as fixed-capital investments has created an upsurge in the demand for servicing volume. Some major brokerage firms now trade servicing portfolios like financial instruments. In the past 12 months, approximately $25 billion dollars worth of servicing has changed hands as a result of mergers and acquisitions of firms with substantial servicing portfolios. The Government National Mortgage Association (GNMA) reports that $22 billion worth of servicing of FHA/VA (Federal Housing Administration/Veterans Administration) loans backing GNMA MBSs, (mortgage-backed securities) were involved in changes of servicer of record in fiscal 1984.

The growth in demand for servicing has driven prices paid for servicing portfolios up. Prices for servicing portfolios have recently run as high as 2½ to 3 points compared to the traditional price of one point, which was the norm well into the early 1980s.

The growing interest in servicing portfolios and their importance as a key factor in a firm's profit calculation make the analysis of the income and expense of the servicing operation extremely important. This is especially true for the period covered in this study, 1979 through 1983, a period of high inflation, emerging delinquency and foreclosure problems and the introduction of new instruments into firms' portfolios.

The most extensive available source of comparative servicing cost and income data for mortgage banking firms is Income and Cost for Origination and Servicing of 1- to 4-Unit Residential Loans, 1983 *soon to be published by the Mortgage Bankers Association of America (MBA). Based on data collected in the annual "Cost Study" surveys, the most recent study covers the years 1979 through 1983. Firms responding to the survey accounted for more than 30 percent of total dollar volume serviced by mortgage bankers in each of the five years. In 1983, survey respondents' total servicing portfolios represented 42 percent of the dollar volume of all 1- to 4-unit nonfarm residential mortgage loans serviced by mortgage bankers. Much of the following is based on data that will be reported fully in the MBA "Cost Study."*

Mortgage bankers experienced increased competition in the servicing of mortgage loans, as well as a changing market environment and structural changes within the industry over the five years surveyed. The emerging trend on the part of some companies to purchase servicing rather than to originate it, together with the increasing tendency of originators to accept lower servicing fees, has resulted in a decline in profit margins and net servicing income per dollar serviced. The trend toward specialization in the servicing area by some mortgage banking firms is perhaps best illustrated by the increasing share of total costs attributable to the amortized cost of purchased servicing. These costs rose to 21.4 percent of total servicing expenses in 1983 compared with their 13.5 percent share in 1979. (See Table 1). Further, there is every indication that the trend on the part of many firms to increase their servicing portfolios through acquisitions will continue.

Servicing fees as a percent of dollar serviced were found to have declined in 1983 as reported by survey respondents. Part of the decline could be attributed to the growing practice of fee splitting, often with an affiliated firm for whom a portfolio is serviced. However, the remainder was the result of competitive pressure on fees as firms continued to add significantly to servicing portfolios.

Personnel costs, the dominant cost factor in the servicing sector, rose substantially from year to year in the period studied. However, because personnel costs moved in tandem with average loan size, personnel expense as a percent of dollar serviced remained hardly changed over the entire interval. Also, personnel costs as a percent of net servicing expense (gross servicing expense minus the amortized cost of purchased servicing) showed a gradual decline over the survey period.

The servicing of 1- to 4-unit residential mortgage loans is an activity that is currently in a period of transition and structural change. A consideration of the data generated by the "Cost Study"

continued

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surveys could clarify the nature of the change and identify the most important trends.

Servicing Income

In the inflationary environment of 1980, servicing income and expenses increased sharply but at roughly the same rate, leaving net income per loan virtually unchanged. The average loan-amount-serviced[1] increased to $25,933.24, a 14.9 percent rise over the 1979 figure. (See Table 2). That caused an 18 percent increase in servicing fee per loan, which in turn, translated into a 19 percent increase in net servicing income per loan to $65.26 compared with the 1979 figure at $55.00 (See Tables 3 and 6). Profit margin on servicing reached 54.5 percent, a slight improvement over the 54.4 percent recorded in 1979.

Much of the increase in servicing expense per loan observed in 1980 was due to a rise in the amortized cost of purchased servicing, which accounted for $4.00 of the $8.09 increase in servicing expenses per loan registered. (See Table 1). The increase to $10.25 in 1980 from the $6.25 level of 1979 represented a 64 percent increase in this cost category and increased its share of total expenses to 18.9 percent in 1980 from 13.5 percent in 1979. On an industry-wide basis, mortgage bankers increased their servicing portfolios by 128 percent of their 1980 originations. Service corporations of savings and loan institutions appear to have been particularly active in acquiring loans servicing-released during this period.

Dr. Victor Cholewicki is an assistant economist for the Mortgage Bankers Association. He received his Ph.D. in Economics from Brown University. Before joining MBA, Dr. Cholewicki served on the faculty at Boston University and at the Catholic University of America.

"Some major brokerage firms now trade servicing portfolios like financial instruments. In the past 12 months, approximately $25 billion dollars worth of servicing has changed hands as a result of mergers and acquisitions of firms with substantial servicing portfolios."

Net servicing expense per loan increased 10.2 percent to $44.13 in 1980, due primarily to an increase in personnel and occupancy expenses. (See Tables 1 and 5). Compensation per employee ballooned to $14,745.80, a 16.8 percent jump from the $12,686.80 level of the previous year. However, due to the surge in average loan size serviced, the net servicing expense ratio (net servicing expense as a percent of dollar serviced) actually fell to .1702, the lowest level for this entity in the five years surveyed.

Key variables

Most of the key variables in servicing activity held remarkably steady in 1981. Servicing income per loan rose 5.3 percent while expenses rose 7.9 percent. The result was a 3.1 percent rise in net servicing income per loan to $67.31. The increase in income per loan was attributable to an increase in average loan size serviced of 6.9 percent. However, this was somewhat offset by a decline in servicing fee as a percent of dollar serviced to .3956, down from .4018 the year before. The increase in expense was due almost entirely to a 5.6 percent rise in the average compensation of servicing personnel, which was the primary cause of a 9 percent increase in net servicing expense per loan. Amortized cost of purchased servicing was not a major factor in the increase in servicing costs in 1981. This entity rose

continued

TABLE 1

Servicing Expenses Per Loan*

Expenses	1979	1980	1981	1982	1983
Personnel	$22.28	$24.73	$26.41	$29.12	$33.66
Pct. Incr. Over Prev. Yr.	—	11.0	6.8	10.3	15.6
Occupancy	$ 1.91	$ 2.18	$ 2.83	$ 3.08	$ 3.48
Pct. Incr. Over Prev. Yr.	—	14.1	29.8	8.8	13.0
Other Direct	$11.45	$11.50	$13.20	$16.54	$15.78
Pct. Incr. Over Prev. Yr.	—	0.0	14.8	25.3	(4.6)
G&A (Net of Am. Cost of Purch. Servicing)	$ 4.42	$ 5.72	$ 5.67	$ 6.40	$11.72
Pct. Incr. Over Prev. Yr.	—	29.4	(0.9)	12.9	83.3
Amortized Cost of Purchased Servicing	$ 6.25	$10.25	$10.58	$15.03	$17.88
Pct. Incr. Over Prev. Yr.		64.0	3.2	42.1	19.0
Total Gross Expenses	$46.29	$54.38	$58.69	$70.19	$83.52
Pct. Incr. Over Prev. Yr.	—	17.5	7.9	19.6	19.0
Percent of Total Gross Expenses					
Personnel	48.1	45.5	45.0	41.5	40.3
Occupancy	4.0	4.0	4.8	4.4	4.2
Other Direct	24.8	21.1	22.5	23.6	20.1
G&A (Net of Am. Cost of Purch. Servicing)	9.6	10.5	9.7	9.1	14.0
Amortized Cost of Purchased Servicing	13.5	18.9	18.0	21.4	21.4

*For definitions of categories see Table 6.

a mere 3.2 percent per loan for survey respondents in 1981, which was the only year of the five surveyed in which mortgage bankers industry-wide added less to their servicing portfolios in terms of dollar volume than they originated.

Although net income per loan rose slightly, profit margin suffered a mild decline, falling to 53.4 percent in 1981 compared to the 54.5 percent recorded in 1980.

Delinquencies and foreclosures emerged as important factors in 1981, as rates for both increased significantly. Net loss on foreclosures leaped to $0.92 per loan in 1981, up 475 percent from the 1980 figure of $0.16. The upward racheting of this figure signalled the beginning of the foreclosure problems facing the mortgage lending industry today. This item would continue to rise significantly in subsequent survey years.

Personnel

Servicing expense per loan soared 20 percent to $70.19 in 1982 compared with the $58.68 figure recorded in 1981.

"The emerging trend on the part of some companies to purchase servicing rather than to originate it, together with the increasing tendency of originators to accept lower servicing fees, has resulted in a decline in profit margins and net servicing income per dollar serviced."

This was partly due to a 5.6 percent rise in compensation per servicing personnel to $15,567.80 in 1982 up from $14,745.80 in 1981, together with a slight but significant decline in number of loans serviced per servicing employee. The result was 10.3 percent increase in personnel expense per loan serviced over the 1981 level. Personnel expense as a percent of dollar serviced rose to 9.5 basis points compared with the 9.2 basis point figure of the previous year.

Another significant source of cost inflation in 1982 was other direct expenses—the office supplies, equipment and services necessary to do business. Other direct expenses per loan rose 25.3 percent in 1982 to $16.54 compared with the 1981 level of $13.20. The increase was spread evenly through almost all categories. The sudden jump of this expense category, which grew at a "normal rate" in the previous survey years, could reflect a basic change in the way firms did business, perhaps a change in the mix of loans that they were servicing, e.g., a greater proportion of adjustable rate mortgages (ARMs). (The servicing of ARMs requires more contact with the borrower.) The slight decline in number of loans serviced per servicing employee would also fit this scenario. Most of the

continued

TABLE 2

Servicing Fee	1979	1980	1981	1982	1983
Average Servicing Fee Per Loan	$ 88.19	$ 104.19	$ 109.64	$ 118.06	$ 123.23
Pct. Incr. Over Prev. Yr.		18.1	5.2	7.7	4.4
Average Servicing Fee As Percent of Dollar Serviced	.3908	.4018	.3956	.3988	.3752
Pct. Incr. Over Prev. Yr.		2.8	(1.5)	0.8	(5.9)
Average Size Loan Serviced[1]	$22,568.87	$25,933.24	$27,715.17	$29,604.21	$32,842.55

TABLE 3

Servicing Income and Expense, Per Loan, for 1- to 4-Unit Mortgage Loans Serviced

	1979	1980	1981	1982	1983
Servicing Income	$101.29	$119.64	$125.99	$138.66	$144.92
Servicing Expense	$ 46.29	$ 54.38	$ 58.68	$ 70.19	$ 83.53
Net Servicing Income	$ 55.00	$ 65.26	$ 67.31	$ 68.47	$ 61.39
Margin	54.3%	54.5%	53.4%	49.4%	42.4%
Percent Change From Prior Survey Year					
Servicing Income		18.1	5.3	10.1	4.5
Servicing Expense		17.5	7.9	19.6	19.0
Net Servicing Income		18.7	3.1	1.7	(10.3)
Income As Percent of Dollar Serviced	.4488	.4603	.4546	.4684	.4413
Net Servicing Income As Percent of Dollar Serviced	.2437	.2516	.2429	.2313	.1869

TABLE 4

Net Servicing Expense	1979	1980	1981	1982	1983
Servicing Expense Minus Amortized Cost of Purchased Servicing	$40.04	$44.13	$48.11	$55.14	$65.65
Pct. Incr. Over Prev. Yr.		10.2	9.0	14.6	19.1
Servicing Expense Minus Amortized Cost of Purchased Servicing As Pct. of Dollar Serviced	.1774	.1702	.1736	.1863	.1999

items in this category would continue to show slower but still vigorous growth in the subsequent survey year.

The other important factor in the increase in servicing expense per loan observed in 1982 was the sharp rise in the amortized cost of purchased servicing. This cost component reached $15.03 per loan in 1982 compared with the $10.58 figure of 1981, a 42 percent increase. The share of total servicing cost represented by the amortized cost of purchased servicing rose to 21.4 percent in 1982, up significantly from the 18 percent share recorded the previous year. Substantial increases in this cost category were registered by firms controlled by bank holding companies and by other controlled subsidiaries. Industry-wide, mortage bankers added to their servicing portfolios by a dollar amount 39 percent larger than their own origination volume in 1982.

continued

TABLE 5

Servicing Personnel

	1979	1980	1981	1982	1983
Number of Loans Serviced Per Servicing Employee	591	602	617	611	582
Pct. Incr. Over Prev. Yr.		1.8	2.5	(0.9)	(4.8)
Average Compensation, Servicing Personnel	$12,686.80	$14,745.80	$15,567.80	$17,083.90	$18,579.40
Pct. Incr. Over Prev. Yr.		16.8	5.6	9.7	8.8
Servicing Personnel Expense As Percent of Dollar Serviced	.0923	.0888	.0920	.0952	.0973
Personnel Expense As Percent of Net Servicing Expense	55.6	56.0	54.9	52.6	51.3

TABLE 6

Income Statement: Servicing, Average Firm, 1979-1983

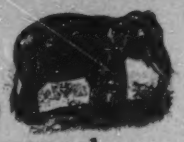
	1979	1980	1981	1982	1983
INCOME:					
Servicing Fee, First Mortgage Loans	$ 88.15	$103.48	$109.21	$117.57	$122.91
Servicing Fee, Non-First Mortgage Loans	.04	.71	.43	.49	.32
All Other Loan Admin. Income					
Other Loan Admin. Income	12.00	13.87	15.29	18.59	22.12
Net Gain or Loss on Foreclosures	(.28)	(.16)	(.92)	(1.11)	(1.75)
All Other Operating Income	1.37	1.74	1.98	3.12	1.32
TOTAL GROSS SERVICING INCOME	101.28	119.64	125.99	138.66	144.92
Expenses					
PERSONNEL:					
Loan Administration	18.35	20.46	21.55	23.14	27.18
Mgt. Not Classified Above	.25	.27	.26	.18	.07
Directors	.00	.00	.00	.02	.36
All Others	.35	.43	.68	1.13	.84
Employee Fringe Benefits	3.33	3.57	3.92	4.65	5.21
OCCUPANCY	1.91	2.18	2.83	3.08	3.48
OTHER DIRECT:					
Edp Svc. Charge & Rentals	5.03	4.25	5.57	6.78	5.69
Other Equipment Rentals	.67	.77	.75	1.10	1.30
Postage	1.55	1.55	1.71	2.04	2.20
Telephone & Telegraph	2.00	2.31	2.52	3.33	3.79
Office Supplies	1.47	1.73	1.71	2.13	2.60
Travel & Entertainment	.41	.51	.55	.80	.76
Automobiles	.29	.36	.35	.28	.35
Advertising	.02	.02	.04	.08	.09
G&A:					
Legal & Auditing Fees	.28	.55	.52	1.48	.77
Provision for Loan Losses	.29	.48	.86	(0.09)	2.43
All Other Operating Expenses	3.85	4.69	4.29	5.01	8.52
AMORT. COST OF PURCHASED SERVICING	6.25	10.25	10.58	15.03	17.88
TOTAL GROSS SERVICING EXPENSE	46.28	54.38	58.69	70.19	83.53
NET SERVICING INCOME	55.00	65.26	67.30	68.47	61.39
Number of Firms	93	99	121	86	113

A further and apparently not fully anticipated increase in foreclosures, resulted in a negative loan loss provision for 1982 of minus $0.09 per loan. Net loss on foreclosures reached $1.11 per loan, up from the $0.92 figure of 1981.

Servicing income per loan increased to $138.66 in 1982, a 10 percent gain over the $125.99 level registered in 1981. This was due to a 6.8 percent increase in average loan size serviced to $29,604.21, and to a 1 percent increase in servicing fee as percent of dollar serviced to .3988. As a result, servicing income as a percent of dollar serviced grew 3 percent to .4684.

Even though net servicing income per loan increased by 2 percent to $68.47 in 1982 compared with the 1981 level of $67.31, alternative measures might suggest a lessening of profitability in servicing. Profit margin dropped to 49.4 percent in 1982 compared with 53.4 percent in 1981, the first time this measure fell below the mid-50s range in the five years surveyed. Also, net income as percent of dollar serviced fell 5 percent in 1982 to .2313, down from the .2429 level of the previous year. Both the precipitous drop in profit margin and the decline in net income as a percent of dollar serviced were sharp departures from the trends of the previous three years.

The seemingly disappointing drop in profit margin and the anemic increase in net income per loan could well be consistent with continued or even increased profitability of servicing, particularly for firms with large volumes of purchased servicing. Purchased servicing yields less net income than servicing on a comparable loan originated by the firm itself due to the fact that the purchase price enters into the cost calculation in the form of the amortized cost of purchased servicing. The larger the percentage of the servicing portfolio that was purchased, the lower will be the net income per loan and profit margin for the entire portfolio. However, providing that the income generated by the loan is greater than the additional expense required to service it (including the amortized cost of purchased servicing) the purchased loan adds to total profit.



"Personnel compensation is the most important cost element in the servicing operation, typically accounting for more than half of all expenses, net of the amortized cost of purchased servicing."

For purposes of the income statement, servicers who originate all of their own servicing show additions to the portfolio to their servicing operation as being free of charge. However, in most cases the origination operation generates negative net income in the loan production process, which is, in effect, the price the firm pays to add to its servicing portfolio. Relying only on the servicing operation's income statement to determine the effects on profitability of purchasing servicing provides a somewhat distorted picture—it underestimates the benefits of the purchased servicing portfolio. The fact that the purchase of servicing avoids losses on origination should be taken into account along with the lower net servicing income per loan generated by the purchased loans. Most originators find that on average it costs them less to originate a loan than to purchase the servicing at market prices. However, there are firms who feel that they can do better by purchasing their servicing rather than by originating it, and have little or no loan production

Table 7

Percent of Survey Respondents' Servicing Volume For Which The Average Servicing Fee As Percent of Dollar Serviced Was Less Than 25 Basis Points

1979	1980	1981	1982	1983
1.2%	3.8%	4.8%	3.3%	10.8%

Table 8

Percent of Conventional Mortgage Loans Originated for 1- To 4-Unit Residential Properties to Total Dollar Volume of Originations by Survey Respondents

1979	1980	1981	1982	1983
27.0%	28%	36.7%	37.9%	40.1%

Profits decline

Most standard measures of servicing profitability declined sharply in 1983. Net servicing income per loan fell 10 percent to $61.39 compared with $68.47 in 1982, the first decline in this measure in the five years surveyed. Net servicing income as a percent of dollar serviced plunged 21 percent in 1983 to .1869, down from .2313 in 1982, intensifying the previous year's trend (see Table 3). Profit margin fell to 42.4 percent, down from the already lowered 49.4 percent figure of 1982.

The major cause of the deterioration of the profitability measures mentioned above was the 6 percent drop in servicing fee as percent of dollar serviced to .3752 in 1983, down from .3988 in 1982, the first significant decrease in this figure in the five years surveyed. The decline in servicing fee largely offset the 10.9 percent increase in average loan size serviced to $32,842.55, up from $29,604.21 in 1982. The result was a modest 4 percent increase in both servicing income and servicing fee per loan as the strong gain in average loan size barely offset the 2.36 basis point drop in servicing fee.

Fee splitting

Part of the observed reduction in servicing fee as a percent of dollar serviced reported by survey respondents may just be a matter of how the fee was entered in the books. It appears that there was a significant increase in fee splitting by 1983 survey respondents. This would explain a portion of the decline. In the 1983 survey, firms reporting average servicing fees as percent of

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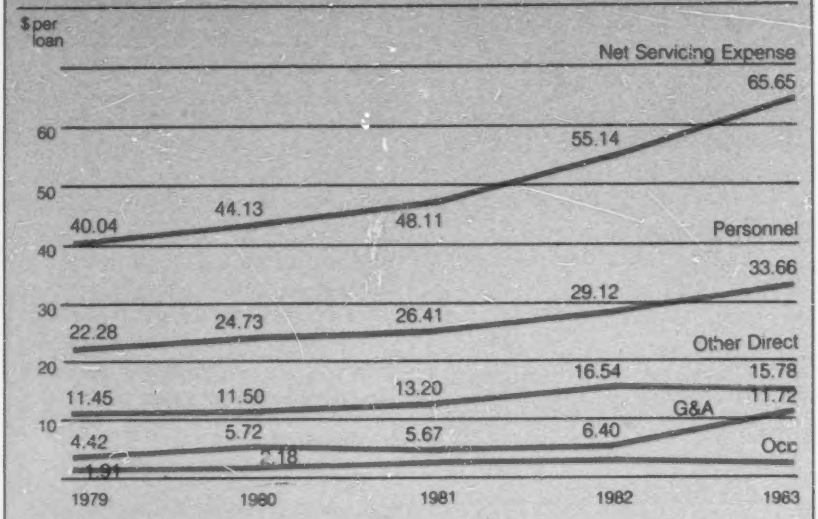
GRAPH 1 SERVICING EXPENSE PER LOAN, AVERAGE FIRM, 1979-1983



GRAPH 2 AMORTIZED COST OF PURCHASED SERVICING PER LOAN, AVERAGE FIRM, 1979-83

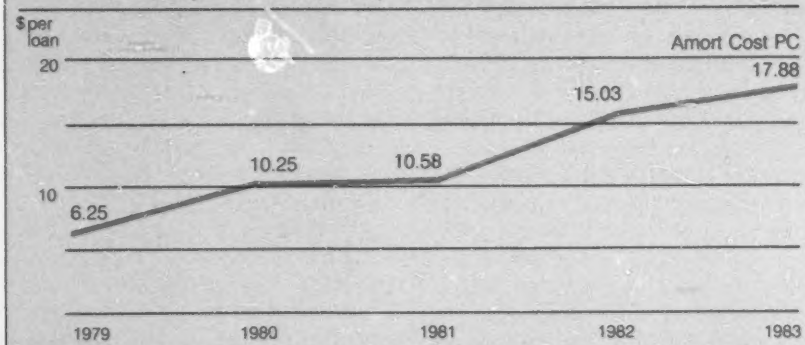


TABLE 9 Average Loan Size Related To Servicing Fees As Percent Of Dollar Serviced, 1983

Number Firms	Servicing Fee Pct. Dollar Loan Amount	Average Loan Size
20	0 to .30	38,846.20
22	.301 to .375	30,506.20
24	.376 to .410	31,582.80
24	.411 to .440	32,575.80
23	GE (greater or equal to) .441	33,926.10

dollar serviced as being less than 25 basis points accounted for 11 percent of the total dollar servicing volume of the survey respondents. This was a dramatic increase over the comparable figure for the 1979 to 1982 surveys that ranged between 1 and 5 percent. Thus, although the servicing fee kept by the servicer may be declining, the total servicing fee paid as a percent of dollar serviced may not be decreasing nearly as drastically. (See Table 7)

Most of the firms receiving less than 25 basis points on their portfolios were efficient servicers of large servicing volume. Many were affiliated with larger parent entitities. On the basis of other indicators, it appears that their loans yielded above average servicing fees but that they retained only a portion on their own servicing income statements.

However, part of the decline in servicing fees observed in the 1983 data represents a real decline in the servicing fee generated by the loan as opposed to the percent of the fee actually entered in the servicers' books. The increasing percentage of conventional loans originated by mortgage bankers may have contributed to this decline. Conventional originations as percent of total dollar volume originated by survey respondents increased from 27.0 percent of 1979 to 40.1 percent in 1983 (See Table 8).

"Part of the observed reduction in servicing fee as a percent of dollar serviced reported by survey respondents may just be a matter of how the fee was entered in the books."

Conventional loans typically have lower servicing fees than the 44 basis point servicing fee available for Ginnie Mae pools.

A further factor could be the increased volume of loans originated with the proceeds of mortgage revenue bonds. Public housing authorities typically offer lower servicing fees. In some jurisdictions, servicing rights are awarded on the basis of competitive bidding. This can result in servicing fees in the low 20s (in basis points). A final factor may have been a reduction in servicing fees offered by builders whose product serves as collateral for homebuyer (builder) bonds.

Administrative expenses

Servicing expense per loan shot up again in 1983, rising 19 percent to $83.53. Net servicing expense also rose 19 percent due primarily to a sharp rise in general and administrative expense as well as an increase in personnel expenses. In addition, the amortized cost of purchased servicing per loan registered a substantial gain.

General and administrative expense per loan jumped 83 percent in 1983 to $11.72 compared with the $6.40 figure recorded in 1982. This was caused by

continued

large increases in both provisions for loan losses and in all other operating expenses. The increase in provision for loan losses to $2.43 per loan, almost three times the highest previous level for this item in the five years surveyed, reflects the onset of delinquency and foreclosure problems. The 1983 figure represented almost 4 percent of net servicing expense, an unprecedented share of expenses for this item in the five years surveyed. The increase in general and administrative expenses that included an increase of $3.51 per loan in the all other expenses category, was responsible for more than half of the increase in net servicing expenses in 1983.

The remainder of the increase in servicing expense was largely attributable to the 15.6 percent increase in personnel expenses per loan to $33.66 compared with $29.12 the previous year. Personnel expenses as percent of dollar serviced also increased, reaching 9.7 basis points. This was caused by an 8.8 percent increase in compensation per servicing employee together with a 4.8 percent decline in the number of loans serviced per employee. Continuing the pattern of the previous year, the fall in the number of loans serviced per servicing employee could reflect both increased delinquency problems faced by firms and a changing mix of loans in portfolio.

Other direct expenses per loan declined slightly, dropping 4.6 percent from the 1982 level. This was due to a large decrease in electronic data processing expenses to $5.69 per loan, down 16 percent from the $6.78 figure of the previous year. The 1983 figure was more in line with the level of the first three survey years than the unusually high level recorded in 1982. The remaining items in the other direct category continued to show vigorous growth though not as strong as in 1982.

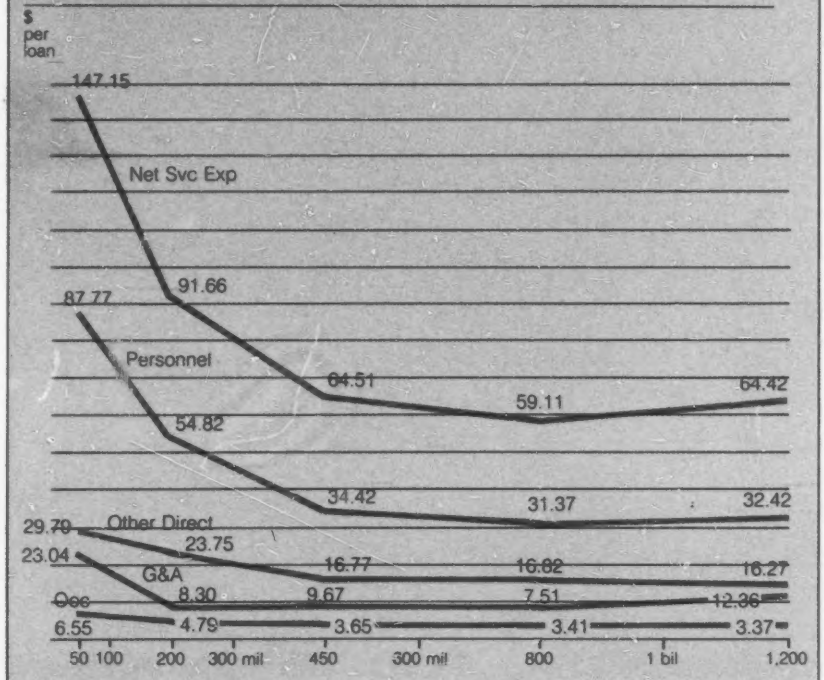
The amortized cost of purchased servicing also increased in 1983, rising to $17.88 per loan, a 19 percent increase over the $15.03 level of the previous year. This was consistent with the industry-wide pattern in which mortgage bankers added 17 percent more to their servicing portfolios than they originated.

TABLE 10 SERVICING INCOME & EXPENSES PER LOAN, GROUPED BY MILLION $ SERVICED, 1983*

Size of Firm Dollar Volume Serviced (in millions)	UNDER $100	$100 to $300	$300 to $600	$600 to $1 Bil.	Over $1,000
INCOME:					
Servicing Fees (on 1st and non-1st mortgages)	$120.29	$128.25	$124.16	$115.91	$123.36
All Other Loan Administration Income	34.01	15.20	26.35	18.80	21.60
GROSS INCOME	154.30	143.45	150.51	134.71	144.96
EXPENSES:					
Personnel	87.77	54.82	34.42	31.37	32.42
Occupancy	6.55	4.79	3.65	3.41	3.37
Other Direct	29.79	23.75	16.77	16.82	16.27
Amortized Cost Of Purchasing Servicing	0.85	1.97	6.35	11.74	20.42
Other G&A	23.04	8.30	9.67	7.51	12.36
GROSS EXPENSES	148.00	93.63	70.86	70.85	84.84
NET INCOME	6.30	49.82	79.65	63.86	60.12
Average Loan Size Serviced	$22,648	$32,968	$32,447	$31,858	$33,090
Servicing Fee as percent of dollar serviced (in basis points)	53	39	38	36	37
Net Servicing Expense	$147.15	$91.66	$64.51	$59.11	$64.42
Number of Loans Serviced Per Servicing Employee	225	287	637	619	601
Number of Firms	14	17	26	15	41

*For definitions see Table 6

GRAPH 3 SERVICING EXPENSE PER LOAN GROUPED BY DOLLAR VOLUME SERVICED, 1983



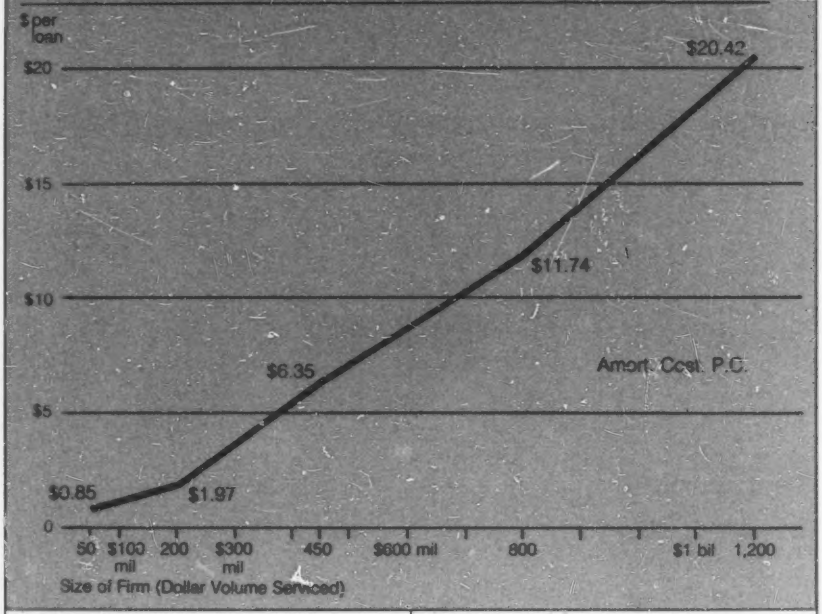
Major components

Focusing on the major component parts of the servicing operation: fees, personnel expense and the amortized cost of purchased servicing could help determine some of the principal factors underlying each. Most of the illustrations draw on 1983 data.

By far the largest part of servicing income is derived from servicing fees, mainly on first mortgages. The magni-

continued

GRAPH 4 AMORTIZED COST OF PURCHASED SERVICING PER LOAN, GROUPED BY DOLLAR VOLUME SERVICED, 1983



tude of these fees, per loan, is determined by the servicing fee as percent of dollar serviced and by the average dollar loan amount. The data suggest that portfolios with very low servicing fees as percent of dollar serviced (less than 30 basis points) were associated with high loan amounts. (See Table 9). However, for portfolios with servicing fees averaging more than 30 basis points, higher servicing fees as percent of dollar serviced tended to correspond with somewhat higher average loan sizes. The high average loan amount associated with servicing fees less than 30 basis points reflects the incidence of fee splitting.

A remarkably high degree of similarity was found to exist in regard to servicing fees for firms with portfolios of more than $100 million. On average, these firms received roughly $120 per loan in servicing fees on first mortgages on loans that averaged about $33,000 in size; that worked out to approximately 37 basis points. (See Table 10). This was very near the industry average. The largest firms, those with portfolios of more than $1 billion, tended to bunch in the middle of the range in both servicing fee as percent of dollar serviced and in average loan amount and consequently in servicing fee per loan. Firms with less than $100 million in servicing, however, tended to have significantly smaller average loan size ($22,648) and higher servicing fees (53 basis points). This suggests that many of these firms have highly seasoned loan portfolios. Also, smaller firms tend to do proportionately more construction lending and originate more second mortgage loans, both of which yield higher servicing fees.

Personnel compensation is the most important cost element in the servicing operation, typically accounting for more than half of all expenses, net of the amortized cost of purchased servicing. This magnitude is determined by the number of loans serviced per servicing employee and by the compensation level. The number of loans serviced per servicing employee tends to be related to dollar volume serviced. Increases in servicing personnel efficiency tend to occur up to the range of $300 to $600 million dollars serviced. (See Table 10). For larger portfolios, the number of loans serviced per servicing employee tends to taper off somewhat. Compensation levels tend to rise as servicing per servicing employee rises, diminishing to some extent the impact of servicing efficiency on personnel expense per loan serviced. The result is that firms with portfolios exceeding $300 million in dollar volume have roughly similar loan administration and net servicing expenses per loan. (See Graph 3 and Table 10). These firms have sharply lower net servicing expenses per loan than firms with servicing portfolios of less than $300 million in dollar volume.

Overall, net servicing expense per loan declines as dollar volume serviced increases, reaching a minimum for portfolios of more than $600 million but less than $1 billion, then rises slightly.

Servicing tends to be purchased by large firms to add to already profitable operations. (See Graph 4 and Table 10). Of the firms with the 35 highest amortized cost of purchased servicing per loan magnitudes, 33 had servicing portfolios in excess of $300 million and of these 22 had portfolios in excess of $1 billion. Further, efficiency in servicing does not appear to have been the primary reason for the firms' decision to purchase servicing. The firms with the 35 highest amortized cost of purchased servicing per loan figures, averaged 587 loans serviced per servicing employee, only 2.3 percent higher than the average for the remaining 78 surveyed firms. Also, the characteristics of the loans purchased servicing-released do not appear to be the determining factor. The firms with the 35 highest amortized cost of purchased servicing per loan figures averaged about the same servicing fee as percent of dollar serviced as the 41 firms that originated all of their own servicing.

Competition in the servicing area can be expected to remain strong. Pressures to reduce servicing fees will continue, as evidenced by the current effort to push the FHLMC servicing fee floor down to 25 basis points from the current 37.5. At the same time, delinquency problems and adjustments to changing portfolio mixes may well have boosted the net servicing expense ratio by 2½ basis points during the 1982 to 1983 period. Nevertheless, servicing can be expected to remain a highly profitable activity for the efficient firm with a low risk portfolio. □

[1] The average dollar loan amount figures have been adjusted to reflect the average principal balance over the course of the year. They are the average of beginning and end of year total dollar loan amount divided by the average of beginning and end of year number of loans serviced. This figure provides a more accurate determination of income and expenses as a percent of dollar serviced. If the end of the year dollar loan amount serviced divided by end of year number of loans serviced were used, it would overstate the average dollar loan amount and therefore understate income and expense as percent of dollar serviced. For reference, the *end of year* average dollar loan amounts are given below:

	1979	1980	1981
End of year average dollar loan amount	$24,137.04	$27,844.83	$28,607.55

1982	1983
$30,478.48	$34,581.95

MORTGAGE MARKET TRENDS

At this time, conventional wisdom holds that despite the upward movement of some economic variables during May, the second quarter's flash estimate for real GNP (gross national product) will be revised downward to about 2 percent from its original rate of 3.1 percent. The flash estimate was based on the expectation that the trade sector would not continue to weaken during the second quarter at the same rate that it had in the first quarter of the year. However, the net export figures reported for April and May show that this is not likely to be the case. For instance, following an $11.9 billion jump in April 1985, the merchandise trade deficit widened by another $12.7 billion in May. The most recent monthly increase, the second largest on record, was mainly due to a surge of imports from Europe.

In broad terms, the root of the problem in the trade sector is the high value of the dollar, which despite some recent downward movement is now approaching the level it was at last summer, when it was judged by some analysts to be overvalued by as much as 40 percent. Although a strong dollar has its advantages, it is detrimental to U.S. trade because it causes foreign-made goods to be relatively less expensive than domestic products and U.S. exports to be relatively more expensive abroad. In addition, another factor exacerbating the trade situation is the weakness in the economies of U.S. trading partners. Due to their slower rate of growth, their imports from the U.S. have been on a declining trend. For example in April and May, U.S. exports fell 3.6 percent and 2.1 percent, respectively.

Although the steady deterioration of the net export picture has stifled economic growth in general, the problems caused by foreign competition are being felt most keenly by the manufacturing sector. It is probable that imports are the main reason that new factory orders have declined in three of the last four months. In the one month they rose, May 1985, the bulk of the increase came from orders for defense related goods, a highly volatile area. Further, after dropping 0.2 percent in April, industrial production fell 0.1 percent in May, leaving it no higher in May than it was in the summer of 1984. Moreover, this drop in industrial production caused another decline in the capacity utilization index, which has been trending downward all year. In May, output at the nation's factories, mines and utilities stood at 80.3 percent. Finally, even though the civilian unemployment rate remained at 7.3 percent for the fifth consecutive month in June, employment in manufacturing actually went down by 45,000 jobs, and since January 1985 has declined by 220,000 jobs. The numerous problems stemming from the interactions of these two sectors (i.e. trade and manufacturing) will probably keep real economic growth in the low to moderate range or around 2.5 percent for the remainder of the year.

Commensurate with the slowdown in economic activity, there has been a sharp drop in both long-and short-term interest rates, with the decline in short-term instruments being more pronounced. For instance, since mid-March short-term rates have fallen by approximately 200 basis points, while yields on long-term securities have dropped by about 150 basis points. Presently, one-year Treasury bills are averaging 7.09 percent, the lowest level they have been in seven years and long-term securities are averaging 10.50 percent. In line with these declines, several administered rates have also fallen during this period. In late May, the Fed cut the discount rate from 8 percent to 7.5 percent and in mid-June, the prime rate was dropped to 9.5 percent. In both cases, this is the lowest these rates have been since 1978. In addition, the VA rate has fallen by a percentage point, from 12.50 percent to 11.50 percent. As expected, conventional mortgage rates have dropped accordingly. Thirty-year fixed-rate mortgages are averaging about 12 percent and adjustable rate mortgages are approximately 150 basis points lower or around 10.50 percent. With economic growth expected to remain sluggish for the rest of the year, interest rates will drop another notch or two over the near-term and then stabilize. Mortgage rates in particular, will remain in the 11.5 percent to 12 percent range.

Propelled by this drop in interest rates, the housing sector has been one of the few bright spots in the economic picture this year. A number of variables seem to best reflect the underlying strength of this area. Foremost among these is new home sales, which rose a seasonally adjusted 9.7 percent in May, to reach an annual rate of 676,000 units. In addition, although existing home sales edged downward by 1 percent in May, all of the drop was concentrated in the South. The other three regions of the country registered sales increases. Even more importantly, despite the decline, the annual sales rate for existing homes remained above the 3 million unit mark for the third consecutive month. Moreover, in May new construction spending rose 1.5 percent and new construction contracts rose 1 percent. The increase in construction spending placed it at a record annual rate of $343.5 billion. Under the projected interest rate scenario, home sales, both new and existing, are expected to remain near their present levels over the near-term. In addition, refinancings should continue at the healthy pace they attained in the second quarter, and housing starts, after falling in May, will pick up again. Overall, this implies that origination activity will be strong through the third quarter and well into the fourth quarter.

Robert M. Rosenblatt
Assistant Economist
July 15, 1985

HOUSING ACTIVITY

RESIDENTIAL STRUCTURES, BY UNIT TYPE

(Units in thousands)

YEAR AND MONTH	HOUSING STARTS						PERMITS 17,000 ISSUING PLACES					
	Actual			Seasonally Adjusted Annual Rate			Actual			Seasonally Adjusted Annual Rate		
	Total	1-4 Units	5+ Units	Total	1-4 Units	5+ Units	Total	1-4 Units	4+ Units	Total	1-4 Units	5+ Units
1985												
JAN	105	66	39	1,849	1,165	684	104	64	40	1,635	1,053	582
FEB	95	68	27	1,647	1,231	416	101	63	38	1,624	1,041	583
MAR	145	101	44	1,889	1,274	615	144	96	48	1,741	1,131	610
APR	175	118	57	1,933	1,268	665	160	105	55	1,704	1,066	638
MAY	169	118	51	1,673	1,149	524	170	109	61	1,778	1,064	714
JUN	163	110	53	1,705	1,126	579	156	99	57	1,713	1,082	631
1983 TOTAL	1,703	1,181	522				1,605	1,035	570			
1984 TOTAL	1,750	1,206	544				1,682	1,065	617			
6 MONTHS												
1985	852	581	271				835	536	299			
1984	915	632	283				894	579	315			
1983	806	566	240				769	503	266			
1982	454	331	123				432	279	153			

RESIDENTIAL STRUCTURES BY REGION

(Units in thousands)

YEAR AND MONTH	STARTS								PERMITS 17,000 ISSUING PLACES							
	Actual				Seasonally Adjusted Annual Rate				Actual				Seasonally Adjusted Annual Rate			
	North East	Mid-West	South	West	North East	Mid-West	South	West	North East	Mid-West	South	West	North East	Mid-West	South	West
1985																
JAN	10	8	56	32	248	270	826	505	13	8	53	31	271	208	699	457
FEB	7	6	50	31	260	185	745	457	11	7	50	33	266	187	678	493
MAR	16	17	74	37	265	290	853	481	20	17	68	39	265	234	750	492
APR	26	22	80	48	293	247	874	519	24	22	71	43	258	223	760	463
MAY	25	28	72	45	239	251	743	440	28	27	72	45	267	263	784	464
JUN	27	27	68	41	289	239	752	425	26	25	64	42	279	253	746	435
1983 TOTAL	168	218	935	382					164	188	863	390				
1984 TOTAL	204	243	866	436					201	212	812	457				
6 MONTHS																
1985	110	108	400	234					122	106	378	233				
1984	86	115	479	235					94	104	442	252				
1983	75	95	456	182					72	82	428	188				
1982	43	60	262	88					44	49	246	92				

HOUSING ACTIVITY (Cont'd.)

YEAR AND MONTH	HOUSING SALES (Units in thousands)				VALUE OF NEW CONSTRUCTION PUT IN PLACE (Dollars in millions)				CONSTRUCTION STATUS (Units in thousands)					
	EXISTING HOUSES[1]	NEW HOMES			Seasonally Adjusted Annual Rate				Under Construction			Completions		
		Sold	Available For Sale	Months Supply at Current Rate	Total	1 Unit	2+ Units	Non-res.	Total	1-4 Units	5+ Units	Total	1-4 Units	5+ Units
1984														
DEC	174	38	358	7.0	$193,037	$82,053	$29,866	$81,118	1,051	620	431	150	104	46
1985														
JAN	190	48	353	6.8	198,623	82,457	30,558	85,608	1,030	597	433	119	84	35
FEB	193	55	349	6.5	197,111	80,919	29,401	86,791	1,001	585	416	121	79	42
MAR	263	67	352	6.4	196,047	81,549	29,286	85,212	1,020	602	418	125	83	42
APR	283	57	361	7.1	202,543	82,851	28,500	91,192	1,067	628	439	126	91	35
MAY$_P$	**294**	**65**	**360**	**6.5**	**202,612**	**83,941**	**29,357**	**92,314**	**1,105**	**661**	**444**	**132**	**84**	**48**
1983 TOTAL	2,719	623										1,393	1,021	372
1984 TOTAL	2,868	639										1,653	1,139	514
5 MONTHS														
1985	1,223	292										623	421	202
1984	1,199	291										603	414	189
1983	1,047	267										447	326	121
1982	756	159										366	250	116

LENDER ACTIVITY

LONG-TERM MORTGAGE LOANS CLOSED

By Type of Institution and By Unit Type

(Dollars in millions)

YEAR AND MONTH	TOTAL					1-4 UNITS				
	Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.	Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.
1984										
AUG	$26,296	$ 3,570	$ 12,532	$ 8,468	$ 1,726	$17,299	$ 3,070	$ 9,546	$ 4,619	$ 64
SEPT	20,860	3,050	9,654	7,278	878	13,369	2,400	6,889	4,023	57
OCT	23,075	3,700	9,643	8,806	926	15,217	3,110	7,188	4,813	106
NOV	21,562	3,370	9,219	7,818	1,155	13,639	3,090	6,445	4,060	44
DEC	28,852	5,250	10,619	9,414	3,569	15,873	4,090	6,914	4,789	80
1985										
JAN$_P$	**n.a.**	**n.a.**	**7,922**	**7,323**	**1,002**	**n.a.**	**n.a.**	**5,722**	**3,927**	**48**
1983 TOTAL	276,371	65,050	103,882	91,500	15,939	193,535	55,680	81,524	55,605	726
1984 TOTAL	297,406	53,160	129,482	97,776	16,988	196,139	44,500	96,187	54,626	826
1 MONTH										
1985	n.a.	n.a.	7,922	7,323	1,002	n.a.	n.a.	5,722	3,927	48
1984	20,601	4,870	7,818	7,158	755	14,144	4,190	5,839	4,067	48
1983	15,616	4,710	4,755	5,371	780	10,695	3,880	3,621	3,146	54
1982	7,691	2,030	2,410	2,471	780	4,991	1,560	1,975	1,440	16

LENDER ACTIVITY (Cont'd.)

LONG-TERM COMMITMENT ACTIVITY

By Type of Institution

(Dollars in millions)

YEAR AND MONTH	5+ UNITS Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.	NONRESIDENTIAL Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.
1984										
AUG	$ 1,595	$ 0	$ 1,221	$ 350	$ 24	$ 7,402	$ 500	$ 1,765	$ 3,499	$ 1,638
SEPT	1,516	70	1,083	339	24	5,975	580	1,682	2,916	797
OCT	1,341	0	880	373	88	6,517	590	1,575	3,620	732
NOV	1,664	0	1,098	455	111	6,259	280	1,676	3,303	1,000
DEC	2,488	80	1,488	488	432	10,491	1,080	2,217	4,137	3,057
1985										
JAN▸	n.a.	n.a.	691	399	102	n.a.	n.a.	1,509	2,997	784
1983 TOTAL	19,443	3,840	8,521	5,485	1,597	63,393	5,530	13,837	30,410	13,616
1984 TOTAL	22,125	1,980	13,160	5,519	1,466	79,142	6,680	20,135	37,631	14,696
1 MONTH										
1985	n.a.	n.a.	691	399	102	n.a.	n.a.	1,509	2,997	784
1984	1,836	320	938	531	47	4,621	360	1,041	2,560	660
1983	1,532	650	529	312	45	3,389	180	605	1,913	757
1982	452	90	168	168	26	2,388	520	267	863	738

YEAR AND MONTH	ISSUED DURING MONTH Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.	OUTSTANDING Total	Mtg. Bankers	S&Ls	Banks[2]	Life Cos.
1984										
AUG	$ 19,793	$ 2,920	$ 12,316	$ 3,682	$ 875	$92,436	$ 7,970	$52,800	$18,655	$13,011
SEPT	17,278	2,910	9,852	3,021	1,495	90,837	8,150	51,666	17,591	13,430
OCT	19,331	3,910	10,578	3,349	1,494	89,826	8,370	50,624	16,996	13,836
NOV	20,830	3,430	11,549	3,317	2,534	92,434	8,190	51,651	19,389	15,204
DEC	22,227	5,480	10,872	3,810	2,065	91,093	8,700	50,483	17,905	14,005
JAN	n.a.	n.a.	9,207	3,548	1,562	n.a.	n.a.	49,556	16,711	14,123
1983 TOTAL	260,343	81,070	123,361	38,195	17,717					
1984 TOTAL	264,193	50,100	146,184	47,065	20,844					
1 MONTH										
1985	n.a.	n.a.	9,207	3,584	1,562					
1984	18,183	4,660	9,173	3,010	1,340					
1983	15,693	7,010	5,555	1,928	1,200					
1982	7,237	2,940	2,261	1,743	293					

MORTGAGE INSURANCE

(Units in thousands, Dollars in millions)

YEAR AND MONTH	APPLICATIONS RECEIVED (Units) Total	FHA**	VA	Private	LOANS INSURED Total Units	Total Amt.	FHA(203) Units	FHA(203) Amt.	VA Units	VA Amt.	Private Units	Private Amt.
1985												
JAN	138	56	12	70	93	5,973	20	1,125	11	723	62	4,125
FEB	138	59	13	66	73	4,787	10	579	13	867	50	3,341
MAR	168	65	16	87	91	5,824	27	1,504	13	826	51	3,494
APR	188	67	19	102	110	7,103	35	2,007	14	944	61	4,152
MAY	189	70	19	100	98	6,429	20	1,185	13	868	65	4,376
1983 TOTAL	1,921	777	261	883	1,302	79,469	367	19,141	283	17,965	652	42,363
1984 TOTAL	1,862	477	180	1,205	1,345	86,777	200	10,644	199	12,730	946	63,403
5 MONTHS												
1985	821	317	79	425	465	30,116	112	6,400	64	4,228	289	19,488
1984	798	198	87	513	570	36,353	102	5,459	99	6,390	369	24,423
1983	755	364	110	281	400	23,253	125	5,959	94	5,935	181	11,359
1982	292	115	41	136	180	9,902	40	1,656	32	1,843	108	6,403

SECONDARY MARKET ACTIVITY

(Dollars in millions)

YEAR AND MONTH	FNMA Portfolio Comm.	FNMA Portfolio Purc.	FNMA Mortgage-Backed Securities Outstanding	FNMA Mortgage-Backed Securities Issued	FHLMC Comm. to Sell	FHLMC Comm. to Buy	FHLMC Mtg. Purc.	FHLMC Mtg. Sold	GNMA Pass-Through Securities Applications	GNMA Pass-Through Securities Issued
1985										
JAN	1,300	1,943	36,915	913	3,030	4,264	2,197	1,984	4,573	2,654
FEB	1,895	1,559	38,508	1,820	3,362	3,622	3,247	2,425	4,182	2,700
MAR	1,636	2,256	39,370	1,087	3,580	3,453	3,232	3,115	3,757	2,772
APR	1,921	1,515	40,952	1,856	4,672	4,141	2,201	1,973	2,230	2,558
MAY	2,074	1,703	41,613	1,004	n.a.	n.a.	n.a.	n.a.	6,073	3,595
JUN	1,593	1,904	42,755	1,519	n.a.	n.a.	n.a.	n.a.	3,324	3,609
1983 TOTAL	18,606	17,558	—	13,081	30,921	32,846	22,952	21,376	70,461	50,495
1984 TOTAL	21,008	16,722	—	13,546	30,743	32,601	21,885	20,489	36,101	27,859
6 MONTHS										
1985	10,419	10,880	—	10,495	*14,644	*13,540	*10,877	*9,497	24,139	17,888
1984	10,117	9,185	—	8,556	6,025	6,430	5,081	3,907	19,004	15,264
1983	9,037	8,988	—	7,388	6,410	7,445	7,754	7,391	37,950	25,781
1982	9,511	4,537	—	3,876	9,178	9,191	6,481	6,483	11,386	6,756

**—FHA Applications Received now includes the Direct Endorsement Program *—4 Months Totals

INTEREST RATES AND YIELDS

YEAR AND MONTH	1- to 4-UNIT MORTGAGES: FHA OPINION SURVEY FHA NEW[3]	CONVENTIONAL New	CONVENTIONAL Existing	FHLBB SURVEY CONVENTIONAL New	CONVENTIONAL Existing	FNMA Manndatory Delivery Yields ARM (5 yr. Treas.)	Conv.	APARTMENTS[4]
1985								
JAN	13.01%	12.88%	12.88%	12.27%	12.61%	12.400%	12.650%	13.72%
FEB	13.27	13.06	13.06	12.21	12.39	12.238	12.675	14.54
MAR	13.43	13.26	13.28	11.92	12.19	12.860	13.070	14.60
APR	12.97	13.01	13.01	12.05	12.11	12.525	12.669	14.16
MAY	12.28	12.49	12.50	12.06	12.09	12.038	12.281	13.34
JUN	n.a.	n.a.	n.a.	11.75	11.76	11.125	11.600	13.38

YEAR AND MONTH	CURRENT SECONDARY MARKET YIELDS: GNMA[5]	FNMA[5]	FHLMC[5]	SELECTED SECURITIES: A-Rated[6] Utility	U.S. Government 10-yr.	U.S. Government 26-wk.	Prime Comm. Paper 90-119 Days
1985							
JAN	12.35%	—	—	12.78%	11.38%	8.00%	8.03%
FEB	12.42	—	—	12.76	11.51	8.39	8.54
MAR	12.77	—	—	13.17	11.86	8.90	8.90
APR	12.44	—	—	12.75	11.43	8.31	8.37
MAY	11.89	—	—	12.25	10.85	7.65	7.83
JUN	11.20	11.20	11.23	11.62	10.16	7.09	7.35

YEAR AND MONTH	SPREADS (Basis Points): FHA New Minus A-Utility	GNMA Minus 10-Yr. Govt.	FNMA Minus 10-Yr. Govt.	FHLMC Minus 10-Yr. Govt.
1985				
JAN	23	97	—	—
FEB	51	91	—	—
MAR	26	91	—	—
APR	22	101	—	—
MAY	3	104	—	—
JUN	n.a.	104	104	107

n.a —Not available; p—Preliminary

[1] From the National Association of Realtors "Existing Home Sales" series

[2] Mutual Savings Banks and Commercial Banks

[3] Secondary market gross yields

[4] Federal Home Loan Mortgage Corp. Existing Construction only

[5] Securities for 30 day delivery

[6] Prior to January 1984 this rate was for Aaa-rated New Issue Utility Bonds

MORTGAGE BANKING ACTIVITY

LONG-TERM MORTGAGE LOANS CLOSED[1]

YEAR AND MONTH	NOT SEASONALLY ADJUSTED									SEASONALLY ADJUSTED			
		1-4 Units				5+ Units							
	Total	Total	FHA	VA	Conv.	Total	FHA	Conv.	Non-[3] res.	Total[2]	1-4 Units	5+ Units	Non-[3] res.
1984													
JUL	$ 3,760	$ 3,330	$ 800	$ 530	$ 2,000	$ 0	$ 0	$ 0	$ 430	$3,530	$2,960	$ 0	$460
AUG	3,570	3,070	520	380	2,170	0	0	0	500	3,120	2,600	0	510
SEP	3,050	2,400	550	380	1,470	70	70	0	580	3,380	2,500	120	780
OCT	3,700	3,110	820	470	1,820	0	0	0	590	3,600	2,920	0	750
NOV	3,370	3,090	820	470	1,800	0	0	0	280	3,890	3,610	0	280
DEC	**5,250**	**4,090**	**1,280**	**690**	**2,120**	**80**	**0**	**80**	**1,080**	**4,880**	**3,860**	**70**	**770**
1983 Total	65,050	55,680	20,620	12,570	22,490	3,840	810	3,030	5,530				
1984 Total	53,170	44,500	10,850	7,130	26,520	1,980	120	1,860	6,680				
12 MONTHS[5]													
1984	53,170	44,500	10,850	7,130	26,520	1,980	120	1,860	6,680				
1983	65,050	55,680	20,620	12,570	22,490	3,840	810	3,030	5,530				
1982	29,250	24,440	8,510	5,160	10,770	1,580	640	940	3,230				
1981	33,470	25,830	8,380	6,200	11,250	1,740	770	970	5,910				

COMMITMENT ACTIVITY: LONG-TERM MORTGAGE LOANS[1]

YEAR AND MONTH	COMMITMENTS DURING MONTH								OUTSTANDING COMMITMENTS END OF MONTH					
	To Borrowers				From Investors				To Borrowers			From Investors		
	Total	1-4 Units	5+ Units	Non-[3] res.	Total	1-4 Units	5+ Units	Non-[3] res.	1-4 Units	5+ Units	Non-[3] res.	1-4 Units	5+ Units	Non-[3] res.
1984														
JUL	$ 4,060	$ 2,940	$ 0	$1,120	$ 4,050	$ 3,580	$ 20	$ 450	$10,840	$ 70	$570	$9,870	$250	$1,570
AUG	2,920	2,630	0	290	4,220	3,380	10	830	7,430	40	500	7,730	210	1,600
SEP	2,910	2,640	30	240	2,760	2,400	80	280	7,350	300	500	7,460	480	800
OCT	3,910	3,240	0	670	4,550	4,090	30	430	7,660	170	540	8,400	370	740
NOV	3,430	2,820	0	610	3,880	2,760	170	950	7,460	40	690	6,940	270	1,050
DEC	**5,480**	**4,090**	**430**	**960**	**4,850**	**3,910**	**80**	**860**	**7,850**	**100**	**750**	**7,810**	**260**	**1,170**
1983 TOTAL	81,070	67,740	4,310	9,020	79,450	64,240	5,770	9,440						
1984 TOTAL	50,100	41,420	510	8,170	55,550	43,820	3,160	8,570						
12 MONTHS[5]														
1984	50,100	41,420	510	8,170	55,550	43,820	3,160	8,570						
1983	81,070	67,740	4,310	9,020	79,450	64,240	5,770	9,440						
1982	47,800	36,760	3,330	7,710	46,740	34,380	3,960	8,400						
1981	36,700	30,170	1,200	5,330	44,700	30,410	1,740	12,550						

OUTSTANDING END OF MONTH INVENTORY

YEAR AND MONTH	Total	1-4 Units				5+ Units			Non-res.[3]
		Total	FHA	VA	Conv.	Total	FHA	Conv.	
1984									
JUL	$8,870	$6,990	$1,480	$1,090	$4,420	$730	$0	$730	$1,150
AUG	7,070	5,520	1,060	740	3,720	640	0	640	910
SEP	7,390	5,490	1,010	680	3,800	640	0	640	1,260
OCT	8,060	6,350	1,190	870	4,290	600	0	600	1,110
NOV	8,010	6,280	1,190	850	4,240	590	0	590	1,140
DEC	**6,840**	**6,090**	**1,500**	**980**	**3,610**	**170**	**0**	**170**	**580**

MORTGAGE BANKING ACTIVITY (Cont'd.)

YEAR AND MONTH	COVERAGE[4] 1-4 Units	5+ Units	Non-[3] res.	SERVICING VOLUME[1] Total	1-4 Units	5+ Units	Non.[3] res.	NOTES PAYABLE[1] (End of Month Balances) Total	Comm. Paper	To Banks	To Others
1984											
JUL	55%	31%	91%	$421,420	$317,600	$63,980	$39,840	$41,960	$6,190	$12,710	$23,060
AUG	60	31	113	363,570	282,400	42,060	39,110	47,940	5,750	13,220	28,970
SEP	58	51	45	381,070	302,840	39,300	38,930	59,220	4,520	14,240	40,460
OCT	60	48	45	417,780	339,960	40,660	37,160	57,230	4,830	17,070	35,330
NOV	51	43	57	422,490	350,580	39,790	32,120	54,180	4,820	19,180	30,180
DEC	56	96	88	385,270	321,620	33,110	30,540	42,280	8,390	23,680	10,210

CONSTRUCTION AND LAND LOAN ACTIVITY[1]

YEAR AND MONTH	CONSTRUCTION LOANS CLOSED Total	1-4 Units	5+ Units	Non-[3] res.	DISBURSEMENTS DURING MONTH Total	1-4 Units	5+ Units	Non-[3] res.	Land Loans	END OF MONTH INVENTORY Total	1-4 Units	5+ Units	Non-[3] res.	Land Loans
1984														
JUL	$790	$130	$210	$450	$280	$ 70	$10	$200	$180	$2,760	$ 900	$240	$1,620	$1,120
AUG	410	110	130	170	100	60	0	40	90	2,200	790	190	1,220	830
SEP	440	100	160	180	100	50	10	40	120	2,150	790	180	1,180	800
OCT	400	210	100	90	90	40	10	40	130	2,180	780	220	1,180	870
NOV	210	140	50	20	170	110	20	40	240	3,520	1,380	410	1,730	2,260
DEC	470	270	120	80	430	220	30	180	470	9,240	3,790	790	4,660	3,440

COMMITMENTS TO BORROWERS: AND LAND CONSTRUCTION LOANS[1]

YEAR AND MONTH	ISSUED DURING MONTH Total	1-4 Units	5+ Units	Non-[3] res.	END OF MONTH BALANCES Total	1-4 Units	5+ Units	Non-[3] res.
1984								
JUL	$1,730	$130	$ 60	$1,540	$4,090	$870	$470	$2,750
AUG	770	190	80	500	3,680	850	460	2,370
SEP	760	100	80	580	4,170	760	580	2,830
OCT	710	150	160	400	3,820	860	590	2,370
NOV	380	140	70	170	3,230	680	430	2,120
DEC	790	200	10	580	3,910	930	280	2,700

Notes: [1] All dollar amounts are in millions.

[2] Total is seasonally adjusted separately from components. Total, therefore, may not equal sum of parts.

[3] Series labeled non-residential are also inclusive of farm data.

[4] Percent coverage equals outstanding commitments received from investors divided by the sum of outstanding end of month inventory and outstanding commitments issued to borrowers, all multiplied by 100.

[5] Year-to-date seasonally adjusted series not calculated.

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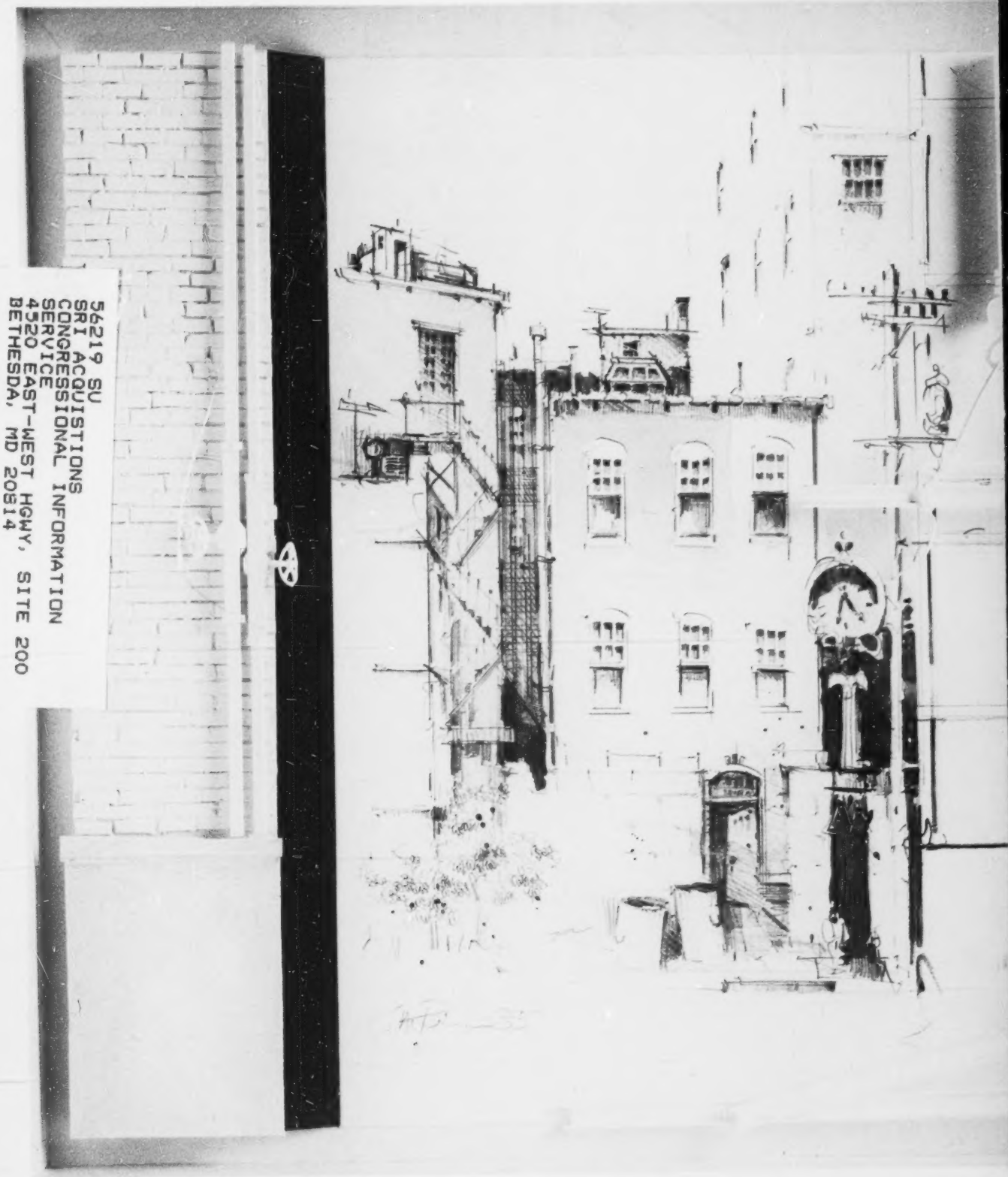
MORTGAGE BANKING

SEPTEMBER 1985

The Magazine of Real Estate Finance



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MORTGAGE BANKING

VOLUME 45 NO. 12
SEPTEMBER 1985

ARTICLES

PAGE 9
REAL ESTATE FINANCE THREE PERSPECTIVES
Mortgage Banking talks to three real estate finance industry leaders about their views on changing times and emerging trends.

PAGE 24
THE PROLIFERATION OF MORTGAGE-BACKED SECURITIES
Dr. Joseph Hu
This author predicts that both the volume and the variety of mortgage securities will further proliferate. Growth will depend on the demand for housing.

PAGE 48
FANNIE MAE'S MORTGAGE SOFTWARE UNDER WEIGH
Jeffrey A. Lebowitz
Fannie Mae undertook a technology assessment of lender needs and of the suppliers of mortgage software and recognized it could play an important role in enhancing the efficiency of mortgage operations.

PAGE 58
PRIVATE CONDUITS CARVE A NICHE IN THE MARKET
Deborah Whiteside
In a few short years, the private conduits have multiplied, differentiated and specialized and it is predicted they are here to stay. An overview of the different conduits is presented in this article.

PAGE 66
BRINGING EVERYONE ABOARD
Sandy Kalenik
Participative management involves communications and personal responsibility. A well-trained team backed by innovative leadership can help create future success.

PAGE 77
OPTIONS: GNMA VS. BOND FUTURES
Laurie Goodman
Options on Treasury bond futures can be a viable hedging alternative for mortgage originators. Citicorp has developed a methodology that allows an easy comparison between options on bond futures and options on GNMAs.

PAGE 90
ALASKA: OUT OF THE REAL ESTATE ICE AGE
Lucille Stietz
Less than 1 percent of Alaska has been developed. But it is not all wilderness. Alaska is people and people have housing needs that have to be met and such housing requires financing.

PAGE 101
AUTOMATED LOAN ORIGINATION "THIS BETTER WORK!"
Vic Lanzillotti
The success or failure of automated loan origination is often determined by the time a contract is signed. Several key issues are explored that can help a company evaluate different automated systems.

PAGE 114
USING INFORMATION AS A RESOURCE
John R. Fall
The approach presented in this article analyzes information needs from the management view of a business to be used to develop an information architecture.

PAGE 125
THE APPRAISER: A DIFFERENT PERSPECTIVE
William L. Pittenger, MAI, SREA
Appraising is not an exact science. An appraisal by definition is a supportable defensible estimate of value. It is a combination of science and art used to form an opinion of value.

INTERNAL MANAGEMENT

PAGE 132
TALENT HUNT: HARD WORK OR GOOD LUCK?
Gerard Sans
How do you go about locating the right person you are looking for a particular position? The process should involve some real soul-searching. This article examines various aspects of recruiting.

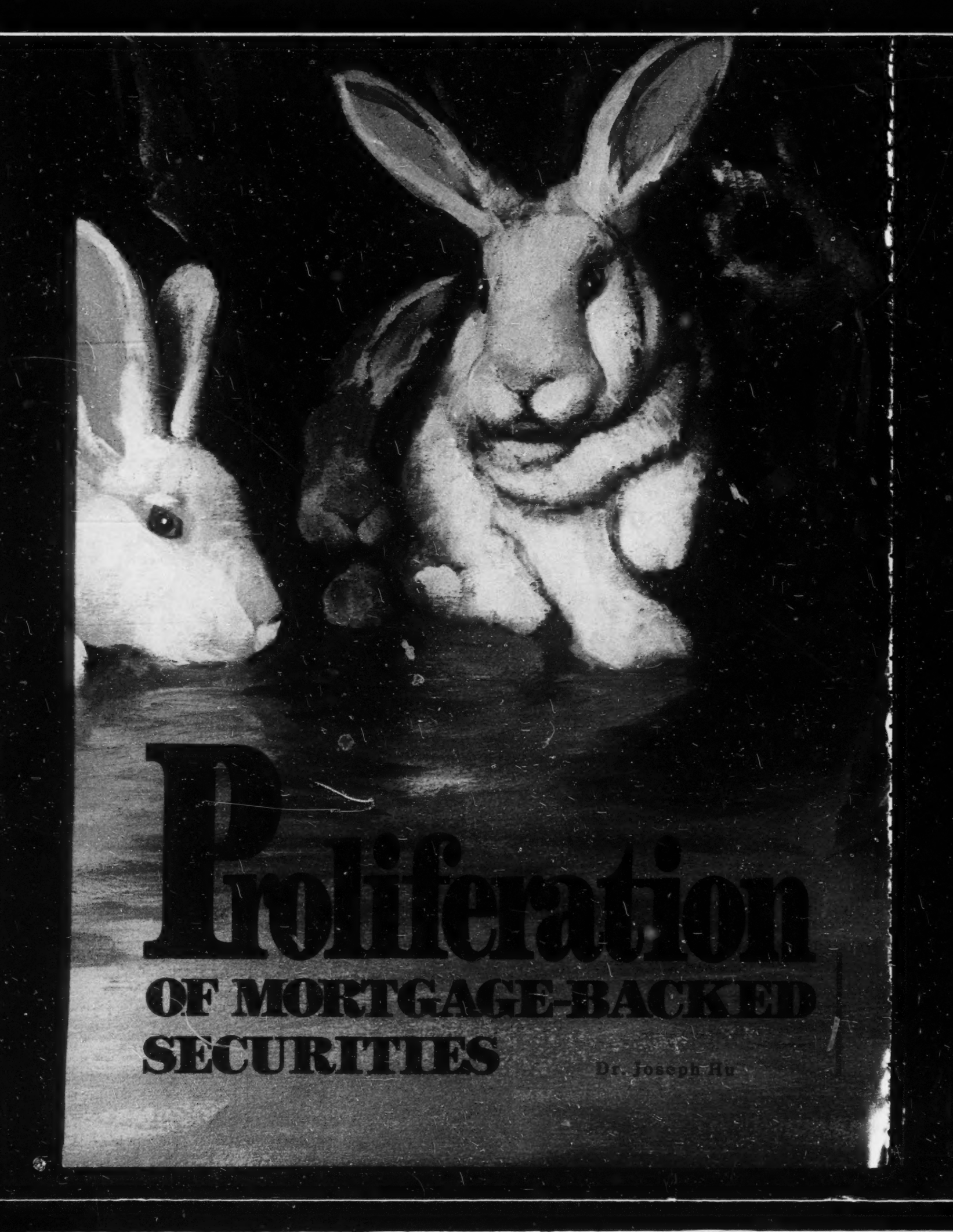
PAGE 145
THE EXECUTIVE INTERVIEW: IT'S NOT THAT SIMPLE
Ken Richardson
In the selection process, the interview is typically the most important tool utilized. Yet few managers have ever received any guidance in how to interview effectively.

PAGE 159
COUNTERATTACK AGAINST THE BANKRUPTCY AMBUSH
Michael S. Polk
Implementation of aggressive and effective procedures to minimize economic losses resulting from bankruptcies is no longer simply desired, it is a necessity for today's lenders and servicers.

PAGE 163
THE LAST WORD (COMMERCIAL PREPAYMENT FEES' NEW LEGAL FRONTIER)
Barrett Sanders
The commercial lending industry's efforts to hedge its mortgage rates by automatic prepayment premiums are just beginning and to date have met a cold shoulder at the courthouse door.

DEPARTMENTS

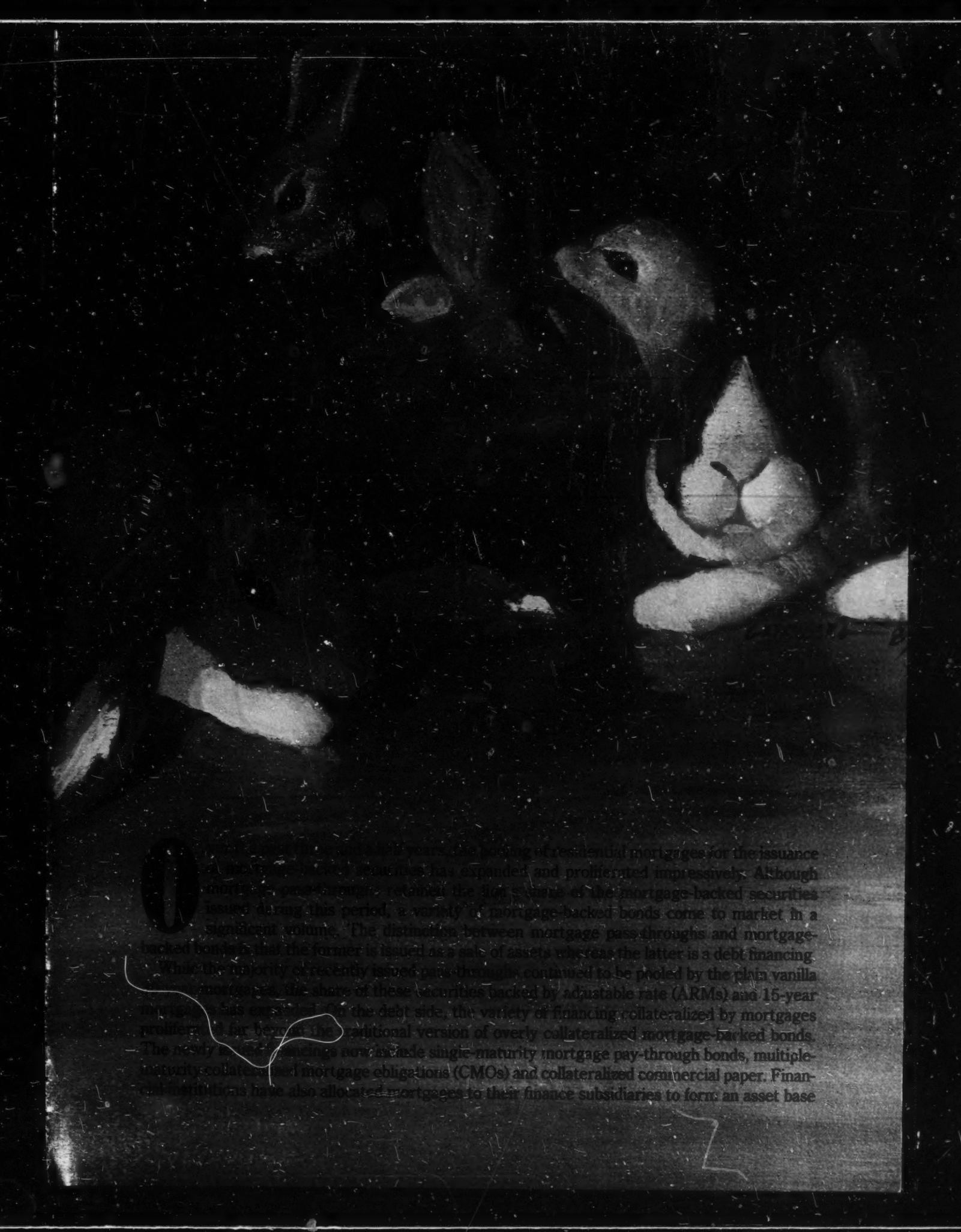
LETTERS	**167**
PEOPLE	**169**
BOOKS	**180**
SECONDARY MORTGAGE MARKETS	**183**
MORTGAGE MARKET TRENDS	**185**
AD INDEX	**199**



Proliferation

OF MORTGAGE-BACKED SECURITIES

Dr. Joseph Hu



for the issuance of adjustable rate or money market preferred stock. In addition to single family mortgages, the collateral now includes multifamily mortgages as well.

Mortgage swap programs at agencies

Mortgage pass-throughs were first issued in early 1970 under a GNMA (Government National Mortgage Association) program whereby mortgage lenders pool their newly originated mortgages and issue pass-through certificates guaranteed by GNMA. These mortgages are either insured by the Federal Housing Administration (FHA) or guaranteed by the Veterans Administration (VA). The GNMA guarantee assures investors that monthly payments generated from the mortgages in the pool are "passed" on to them "through" issuers on a timely basis. The guarantee is backed by the full faith and credit of the U.S. government. In the following year, FHLMC also initiated a similar mortgage security program where FHLMC issues and guarantees its pass-throughs called participation certificates (PCs). With a rare exception, FHLMC PCs are pooled by conventional mortgages (insured by private mortgage insurance companies). In 1977, private entities also began to pool and issue conventional mortgage pass-throughs, although the amount had been quite small. It was not until late 1981 when FNMA, which has been a secondary market portfolio investor all along, initiated a program to issue its guaranteed mortgage-backed securities (FNMA MBSs).[1]

During the 11 years prior to 1982, pass-throughs have been issued mainly in the form of GNMAs and their annual issuance volume rarely exceeded $20 billion. The growth of mortgage pass-throughs, however, exploded in 1982 under FHLMC's Guarantor program and FNMA's newly commenced mortgage-backed security program. Both programs were initially designed to assist thrift institutions (savings and loan associations and savings banks) to restructure and improve the liquidity and marketability of their mortgage portfolios. Under these programs, the two agencies purchase seasoned mortgage loans held by thrifts from the thrifts and simultaneously sell back to the thrifts, agency guaranteed pass-throughs pooled by the same mortgages in the transactions. As a result of this swap, the thrifts would have improved the liquidity and marketability of their mortgage portfolios.

Both programs quickly proved successful. Because they primarily serve thrifts, competition unavoidably emerged for both agencies to make their respective programs more attractive. This competition resulted in many program revisions at the two agencies. For instance, seasoned FHA/VA loans were later included in both programs. While both programs were initially designed to securitize seasoned mortgages, they have increasingly included newly originated mortgages. In fact, newly originated loans have sometimes approached one half of the securities issued under swap programs. In addition, the fee structure, the length of time for commitment periods and options for recourse and delivery have all been revised to give participants convenience and flexibility in securitizing their new and seasoned mortgages.

FIGURE 1A

Annual Issuance of GNMAs, FNMAs, FHLMC PCs
1970-1985

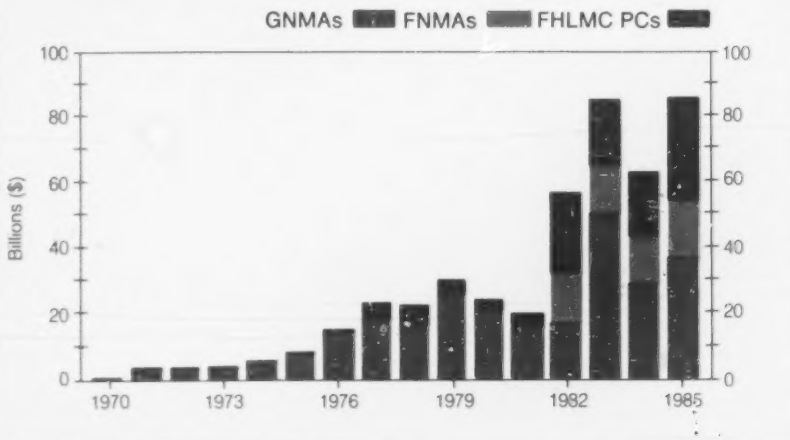


Table 1A

Issuance

	GNMAs ($ billions)	FNMAs ($ billions)	FHLMC PCs ($ billions)
1970	0.5	0	0
71	2.7	0	0.07
72	2.7	0	0.5
73	3.0	0	0.3
74	4.6	0	0.05
75	7.4	0	0.5
76	13.8	0	1.0
77	17.4	0	4.1
78	15.4	0	5.7
79	24.9	0	3.8
1980	20.6	0	2.5
81	14.3	0.7	3.5
82	16.0	14.0	24.2
83	50.5	13.3	19.5
84	27.9	13.5	18.7
85*	36.4	16.2	30.9

*1985 figures annualized based on first six months
Source: GNMA, FNMA and FHLMC

Dr. Joseph Hu is senior vice president and head of the mortgage research and strategy group of the mortgage and thrift department at EF Hutton & Company in New York City, N.Y. Before joining EF Hutton, Dr. Hu was vice president and housing economist in the bond market research department of Salomon Brothers Inc. He has also been an economist in the office of economics with the Federal National Mortgage Association.